

**Opening Statement
Argentina Hearing
February 6, 2002
The Honorable Doug Bereuter
Chairman
Subcommittee on International Monetary Policy and Trade**

The Subcommittee on International Monetary Policy and Trade meets today in open session to examine the financial crisis in Argentina, including the activities of the International Monetary Fund (IMF) within this country. The Subcommittee will hear from the Undersecretary of the Department of Treasury for International Affairs, Dr. John Taylor, on the subject of Argentina, as the Department of Treasury is responsible for implementing U.S. policy towards the IMF.

The Subcommittee on International Monetary Policy and Trade has jurisdiction over international monetary policy generally and the United States participation in the IMF - - both of which are relevant to today's hearing. This is the first hearing, under my chairmanship of this Subcommittee, which addresses the activities of the IMF as it relates to a particular country. Last year, this Subcommittee focused on the regional multilateral development institutions and the Export-Import Bank.

At the outset, I would like to convey to the Subcommittee Members the sensitive nature of the political and economic situation in Argentina. For this reason, I would urge the Members to not focus on the internal workings of the Argentine government. But, to instead focus on the Argentine policies which are relevant to any future IMF or U.S. assistance to the country.

Before introducing our distinguished witness from the Department of the Treasury, I would like to remark upon the overall fiscal situation in Argentina. At each Subcommittee member's desk, the following two products from the Congressional Research Service (CRS) are provided, which I find very instructive: a chronology of relevant events in Argentina and a recent CRS Report on the Argentine Financial Crisis.

The focus of today's hearing is as follows:

1. recent Argentine political and economic history;
2. the recent economic plan supported by the Argentine Government on February 3, 2002;
3. the recent role of the IMF in Argentina;
4. the recommendations of the Meltzer Commission and its dissenting views as it relates to IMF preconditionality criteria for Argentina; and
5. my general views on the IMF.

First, in order to understand the current economic and political turmoil in Argentina, it is necessary to review recent Argentine history. In 1991, the Argentine Government established a currency board to set the peso's value on a one-to-one peg with the U.S. dollar in order to curb hyperinflation. However, because the value of the U.S. dollar appreciated over the past ten years, it became increasingly difficult for Argentina to export its products. As a result, in 1998, Argentina began its fall into a deep recession. By the end of 2001, Argentina had a total debt of approximately \$132 billion.

Furthermore, on November 30, 2001, President de la Rúa of Argentina imposed a \$1,000 per month limitation on personal bank withdrawals. As a result of this restriction and other austerity changes by the Argentine Government, violent protests broke out and President de la Rúa was forced out of office on December 20, 2001. Over the next ten days, there were four different presidents of Argentina, including Mr. Eduardo Duhalde who is currently in power.

When Mr. Duhalde took over as President, he implemented immediate economic reforms. He announced the end of the currency board with its peg to the dollar and his plan for the devaluation of the peso. President Duhalde implemented a dual exchange rate in which the peso was floated for financial transactions, and fixed at a rate of 1.4 pesos to the dollar for foreign trade and certain other transactions. He also continued the freeze of bank deposits in dollars over certain thresholds.

Second, on Sunday, February 3, 2002, the Argentine Government came forth with a new economic plan, which would completely free float the local peso currency and loosen an unpopular freeze on bank accounts. This new economic plan was in part a response to a decision from the Argentine Supreme Court which declared the current freeze on bank deposits to be unconstitutional. To further illustrate the current political and economic instability in Argentina, their Congress is considering impeaching the judges who rendered this decision.

Furthermore, the Argentine Government on February 3rd announced that it would turn all dollar debts into pesos at a rate of one-to-one. This change should help debtors pay back their loans since it will reduce the value of their debt substantially because the floating value of the local peso is at a volatile actual market rate of around two pesos to the dollar. However, both the creditors and the banks will suffer losses because of the pesification of debt. Furthermore, this economic plan also turns all dollar deposits into the local peso at a rate of 1.4 to the dollar. This devaluation of deposits has angered middle class demonstrators because of their loss in savings.

Argentina declared a bank and foreign exchange rate holiday on Monday and Tuesday of this week to prepare for the new economic measures. The effectiveness and political ramifications of these reforms still remains an open question.

Moving on, third -- it is important to note that Argentina has received extensive assistance from the IMF over the past few years. For example, in March 2000, the IMF agreed to a three-year \$7.2 billion arrangement with Argentina. Moreover, in January 2001, the IMF augmented its earlier agreement by pledging another \$7 billion as part of a larger \$40 billion assistance package which involves the Inter-American Development Bank, the World Bank, Spain, and private lenders. However, due to the fiscal instability in Argentina, the IMF withheld its \$1.24 billion loan installment on December 5, 2001.

Fourth, the concept of preconditionality for IMF assistance was endorsed by the majority report of the Meltzer Commission -- a controversial recommendation. I take particular interest in the Meltzer Commission as I am the author of the legislative language, which created this 11-person bipartisan Commission through the FY99 Omnibus Appropriations Act. This Commission, which completed its report in March of 2000, was charged with studying the future of the IMF, the World Bank, and the regional multilateral development institutions. I would encourage the Members and their staff to review both the majority report and the dissenting views of the Meltzer Commission, as I find them very instructive regarding this controversial recommendation.

With respect to the concept of preconditionality for IMF assistance, it appears from press reports that both the IMF and Secretary of the Treasury Paul O'Neill support some form of IMF preconditionality as it relates to Argentina. Examples of preconditionality include the free-floating of the local Argentine peso and the reduction of deficit spending. I do see the merit of a country having a sound economic structure in place before it receives IMF assistance.

However, I also believe that macroeconomic circumstances such as the political and economic repercussions on global stability also need to be taken into account on a case-by case basis by the IMF. A dissenting view of the Meltzer Commission, which Mr. Fred Bergsten of the Institute for International Economics signed, among others, makes this same point. If certain prequalification criteria would have been applied to the 1997 Asian financial crisis (such as with Thailand and Korea), this global contagion may have in fact been worse. As a result of these concerns, I am interested in having Undersecretary Taylor address any degree of regional or global contagion that the Argentine financial crisis might cause or has caused.

Lastly, I would like to offer a few candid remarks on the IMF. A great many in Congress have lost confidence in the IMF. I certainly believe its advice has been both faulty and very dangerous in some instances. Regrettably, I believe that the IMF and the Treasury Department in the last Administration was unwilling to face up to some of its errors and misjudgments in which they exercised a heavy hand. The first step in the process of reform is to face up to recent failures of the IMF and to what I believe has at times been a very serious misuse of its resources. The IMF has been unwilling to do this. The fact is that there were counterproductive IMF policies employed in the early stages of the Asian financial crisis in both Thailand and Korea, treating them like the usual fiscal basketcases which initially they were not. There were also massively wrong-headed loans to Russia, which might better be labeled "Yeltsin loans," and which will be shown, over time, to be part of one of the biggest blunders of the late 20th Century.

At the same time, we, in Congress, need to candidly admit that if we didn't have the IMF or an institution like it, we would have to create one. But we also need to recognize, in reality, that U.S. Treasury has a very large role in greatly influencing and, in reality, practically dictating important IMF policy. The U.S. is, of course, the largest shareholder in the IMF with its 17.16% voting share.

With this background information in mind, I would like to introduce Dr. John Taylor, the Undersecretary of the Treasury for International Affairs, who will, I am sure, assist the Subcommittee in examining these important issues. Dr. Taylor has a very distinguished

academic and professional record. He received his undergraduate degree from Princeton University and his Ph.D from Stanford University. He has taught Economics at Columbia, Yale, Princeton, and Stanford Universities. Dr. Taylor also directed the Monetary Policy Research Program at the Stanford Institute for Economic Policy Research. In addition to these academic positions, Dr. Taylor was a member of the President's Council of Economic Advisers during the Administration of President George Herbert Walker Bush. Moreover, he also served in the private sector as an analyst for Alan Greenspan's Wall Street Firm, Townsend-Greenspan, in the later 1970's and early 1980's, where he studied world commodity markets. Dr. Taylor was sworn into his current position as Undersecretary last year.

Dr. Taylor, we welcome you to this hearing. Without objection, your written statement will be included in its entirety into the record. Before your testimony, I turn to the distinguished Ranking Member of this Subcommittee from Vermont (Mr. Sanders) for any comments that he may have.